4/16/09

Unfortunately I have not been able to attend the previous meetings of the Group. I have reviewed the minutes and public comments on the City's website and attended a Saturday morning workshop on this issue hosted by the Sharpe students at the College. I do feel your Group deserves our highest appreciation for the diligence and thoroughness exhibited in coming to grips with this multi-faceted issue.

I know time is short so I won't comment on the various conduct issues that dominated a significant portion of the Group's discussion.

Instead I wish to address the broader issue of the future character of our residential neighborhoods and how rules regarding the permissible number of renters (students or non-students) can affect investment decisions and the ratio of rental and owner-occupied homes.

Let me start with an anecdote. On a recent trip to Madison Wisconsin, my wife and I walked through a residential area on the lake close to the University campus. We were struck by the fact that virtually all of the homes had been converted to rentals. This included some gorgeous old mansions right on the lake that were basically now fraternity houses. In my view, we need to be careful this does not happen to the City of Williamsburg.

This brings me to economics. The decision factors behind purchasing or upgrading a home for personal use are different than those considered for a rental investment.

An investor is looking to achieve a decent rate of return and cash flow on his investment, taking into account rental income, mortgage costs, taxes depreciation allowances, repairs, improvements, and hoped for eventual capital gain. A homeowner, although enjoying certain tax benefits and hoping for an eventual capital gain, is not expecting positive cash flow from living in his home.

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This different perspective comes into sharper focus for older homes (such as exist near the College) needing renovations and renewal. An investor will usually only undertake renovations if a positive return can be expected. A homeowner makes renovations because he wants to live in a better home. In fact, the expected return on most renovations (including bathrooms and kitchens) is usually well under 100%. Thus, an investor will often avoid renovations or undertake the cheapest approach while a homeowner will often substantially upgrade a home.

This brings me to the 3-person question. As a general rule, the total rent that a property can generate increases with the number of renters legally permitted. This in turn increases the relative value of a house as an investment property as opposed to an owner-occupied property. This is particularly true for a house needing updating and renovation. Such properties are often viewed as cash cows by investors who plan to defer or not update, ~~or~~ while prospective homeowners may shy away unless the property is in a desirable and stable neighborhood.

In conclusion, this issue is broader than mainly a conduct issue. Even if conduct is perfect, the wrong zoning and economic incentives can fairly rapidly turn owner-occupied neighborhoods into rental areas – potentially changing their underlying character.